

BUILDING A CALIFORNIA ECONOMY OF BROAD OPPORTUNITY

**Address by State Treasurer Phil Angelides
New Leaders 9th Annual Awards & Appreciation Luncheon
Los Angeles Marriott Downtown
November 14, 2003**

I have always been told not to be afraid to think “big,” so I want to talk with you today about our priorities in California and the investments we need to make to ensure that we put this State on a sound economic footing in the global economy of the 21st Century.

But in our efforts to think “big,” we should never forget that what really matters is how our priorities and our choices affect people in our own neighborhoods and communities, particularly those who are striving hardest to make the California Dream a reality in their lives.

It’s not possible to talk about broadening economic opportunity without thinking of the people who are struggling every day to build up small businesses, pay the bills, or keep their families together while working crushing hours.

It’s not possible to talk about building a strong economy without hoping that all the children in the State will have the same opportunities that I had and my daughters have had as they prepare to launch out into life.

It’s not possible to talk about creating more livable communities, more vibrant urban villages, without thinking of all the people that we know who spend two or three hours – each direction – commuting to work every day. And seeing them grow tired and weary and disillusioned because they can’t spend more time with their families.

So today, while I am talking about broad ideas and principles and actions we should take to address our big problems, I am thinking about all those people who deserve a chance to share in the promise of mobility and limitless opportunity that is the California Dream.

I would first like to provide a bit of perspective about our State’s economy, because we have had a rugged and grueling journey over the last three years. All of us

have been witness to a world of change. Many of the things that we took as a “given” in the 1990s have been forced to yield to the new realities of the 21st Century.

This is certainly true in the economic realm. All of us, whether we are in the public sector or the private sector, have experienced, firsthand, a roller coaster ride since the century changed. It is unsettling, to say the least, to find that investments that for many years were considered to be traditional, safe, and sound, have turned out to be full of risk.

The stark economic realities brought home to us by the events of the past three years make it imperative that we think in new ways about the public policies and the investment strategies that we need to embrace to ensure sustained economic progress in the years and decades to come. We need to trade in our old conventional wisdom for a new CW, as one of our prominent news magazines expresses it.

I believe that this is the most opportune moment in our modern history to build a new investment dynamic, a dynamic that recognizes the confluence of need for investment in our inner cities and underserved neighborhoods with the great potential for growth and opportunity in those markets. For too many years, the old conventional wisdom in the investment community unfairly characterized our inner cities – our own emerging markets – as places of great risk. But the facts support a new conventional wisdom that our urban neighborhoods – that we too often have thrown away in 25-year cycles – are places of great potential!

Indeed, during the last three years, investments in Main Street businesses in California’s “emerging market” neighborhoods yielded solid returns, while traditional Wall Street investment strategies floundered. It has truly been a time when old myths have been swept away by the facts and experiences of successful reinvestment, from retailers profitably re-entering inner city markets, to lenders who also have found new opportunities there.

Another new CW: Since the economy began to tank more than more than two years ago, we have come face to face with the realization that true wealth in this country is not something that is created in a year. During the boom years, lots of people indulged the notion that somehow, getting rich quick was routine. But more recent events have brought us face to face with the realization that true wealth for any society is something

that is created over the long term. So it is in our best interest for us to begin to think about how we deploy our energies and our assets in a prudent way to create the kind of strong economy we will need to keep us competitive in the years to come.

Over the last two decades, even as our economy has expanded, we have seen an increasing disparity of opportunity that represents a general threat to our economic strength and our social fabric. Because of that threat, center stage in our thinking must now be devoted to ways to create an economy of broad opportunity in this new century. And that should be the goal, not just in California, but all across this country, because in every state and in every region, we see an economy of disparate opportunity that runs counter to the ideals of broad participation and opportunity for all – the most noble tenets of the American free enterprise system.

In California, which in many ways can still be counted as the wealthiest state in the richest nation on earth, we have been witness to a widening economic gap. Despite all of our aggregate success during the go-go years of the '90s in California, we ended the decade with one of five children in poverty. In the San Joaquin Valley – that great swath of fertile farmland between Bakersfield and Stockton – the ratio is one in three.

At the end of that remarkable boom of the 1990s, the median income of the poorest 20 percent in California remained mired at \$14,000 a year – the same level as 1979. If you looked at a map of the State that reflected wealth and income levels, you would see the bright and vibrant colors of places that enjoy economic success. But the map also would be dotted with the duller hues of areas with low incomes and poverty, where families and businesses struggle daily to survive.

I believe this rising disparity presages a two-tier society, with the top tier enjoying the benefits and reaping the rewards of economic progress, while too many of our residents languish in the backwaters of despair. This growing gap in wealth and opportunity diminishes, for everyone, California's economic strength. And, there are direct costs to poverty. Our prison budget alone has soared from \$400 million-a-year in the early 1980s to over \$5 billion this year. But as importantly, this widening chasm of opportunity also speaks volumes about the very nature of who and what we are as a society.

Centuries ago, Aristotle noted that poverty – the absence of a shared stake in society – was the greatest threat to any democracy.

Lester Thurow, the noted MIT professor, has rightly asked, “How does one preach political equality in an economy of ever-growing inequality?”

And here and now in California, we must ask ourselves whether the California Dream can stay alive in a society of “haves” and “have-nots.”

As the State’s chief investment officer, I have always felt it is my obligation not just to be a prudent steward of the resources we have today, but also to think about the investment strategies we need to employ to ensure that we will keep broadening the participation in an economy of sustained strength.

For more than 30 years in California, the issue of growing inequality has been absent from our civic, political and financial discussions. This is a moment of opportunity for us to resurrect that discussion, and to embrace the policies and make the investments that will strengthen California for everyone – not just the privileged few. Now is the time when we must commit ourselves to creating economic prosperity, broadly shared by all Californians – the immigrant’s son or daughter, the single mother struggling to become independent, the day laborer who wants to open a business – everyone who wants a chance to achieve the California Dream.

In order to build an economy of broad opportunity, we must focus our efforts in three key areas.

The first is education – ensuring that in the 21st Century we have a workforce that allows us to enhance our competitive edge in the global economy. The second area that needs our attention is investment in our communities so that we can build the public fabric – the human and physical infrastructure – that will allow California to support a growing population and economy and to maintain the quality of life that is at the heart of our economic strength. The third area is creating the best possible business environment – one that will encourage entrepreneurs, risk-takers, and business owners to set up shop in California, expand their ventures, and create jobs here.

Let me talk briefly about each of these three areas.

The education of our children is the key to our sustained economic progress in an increasingly competitive global economy. We will achieve enduring economic success

only if we have the best-trained workforce that can compete for the high knowledge, high wage jobs at the leading edge of that global economy. It is incumbent on us to make sure that as many Californians as possible have an opportunity to acquire the skills necessary to capture these jobs amidst increasing competition.

In the decades ahead, California will not be the cheapest place to live and work. Although we cannot be blind to the cost of doing business, in the end, we cannot compete for the lowest cost production of goods. That mantle will belong to places like Indonesia, China, Malaysia. Our competitive advantage will be the quality of our workforce and the quality of our enterprise.

In a state where 100 languages are spoken in the schools, where so many children come to the starting line of life so ill prepared to begin the race, we have a Herculean task ahead of us to provide our kids with a first-rate education. It cannot be done by pinching pennies. We cannot be reduced to counting chalk and erasers when our classrooms need advanced technology and skilled teachers.

I will be more specific. We need to demand and expect accountability and results. We need to be willing to experiment with initiatives like urban charter schools. We need to call for more business, parent, and community engagement in our schools. We need the best-trained teachers, the best textbooks and the best technology for our children. And yes, we need to make the financial commitments necessary to ensure that our children are learning.

We don't have our priorities straight. In a \$1.4 trillion economy, our budget debate last year shouldn't have revolved around whether to cut \$1.8 billion from K-12 education – one-tenth of 1 percent of our annual economic output. And it is abominable that we delayed the opening of the new UC-Merced campus – the first UC campus to open in over three decades – to save \$4 million in a \$71 billion State budget.

Now let me speak about investment in our communities. California is a state of 35 million residents today, on the way to 46 million by 2020 and to 59 million by 2040. We must prepare to deal with these growth challenges in a way that preserves our environment and the livability of our neighborhoods – also vital keys to our economic competitiveness.

That means we must have an infrastructure designed to meet the needs of the 21st Century – an infrastructure that supports smart growth and livable communities. Transportation investment that includes transit. Energy investment that includes renewable energy and conservation. Water investment that includes conservation and reuse. And a host of other public endeavors which will ensure that California remains an attractive place to live and work.

Make no mistake about it. The real genius of California after World War II was that we combined strategic public investment and private sector talent and innovation to create the strongest economy in the world.

Our third area of focus must be the fashioning of the best possible business environment that will help to create the jobs and wealth that will sustain us.

This must be a central tenet of any progressive agenda. And I would observe that in the end there is nothing progressive about a workers' compensation system with high premiums and low payouts. There is nothing progressive about liability laws that make it hard for people to build urban condominiums and other multi-family housing – the very kind of housing we need for better growth patterns and the most affordable housing for our young families who are striving to grab the first rung on the homeownership ladder.

In speaking about the need to improve our business climate, I want to emphasize that this is not about simply creating the right kind of business environment for big, multi-national corporations. It is about creating the right kind of environment for the hundreds of thousands of small businesses that are going to forge our future and fuel our economic growth, recognizing that a larger and larger percentage of our economic growth is going to come from our own “emerging markets” – inner cities, women, Latinos, Asians, and African-Americans – that will define California in the 21st Century.

If we are serious about improving the business climate, it means more than freedom from encumbering regulations. It means offering a hand-up – whether it is through small business loans, equity investments or other means – to allow our new California markets to flourish.

We must marry the jet stream of our capital markets with public purpose if we are to strengthen our economy and create the broad opportunity that is our dream. That is why, in May of 2000, we launched a major new investment initiative, *The Double Bottom*

Line: Investing in California's Emerging Markets, calling on both the public and private sectors – public pension plans, state and local governments, as well as the private investment community – to invest in ways that achieve a “double bottom line” of solid returns while also bringing new life and vitality to our less prosperous neighborhoods.

As Treasurer, I have worked hard to provide leadership in this arena. I believe the steps we have taken can be viewed as the four pillars of a new investment dynamic to assist inner-city markets and underserved communities – new models for invigorating elements of our economy that have been too long neglected.

The first pillar is a series of new investment vehicles that move capital to communities and sectors too often overlooked by the old CW. Through our \$250 billion public employee and teacher pension fund portfolios and our \$53 billion State investment portfolio, these new vehicles treat underserved markets as places that will provide solid returns and build our economy rather than as secondary opportunities or as political imperatives.

At the California Public Employees' Retirement System, we have created a \$475 million California Initiative with 10 partners to invest equity to expand inner-city businesses and to give us the returns we need to meet our pension obligations. I am proud to say that our allocation of capital to date has leveraged another \$665 million of capital investment. At the California State Teachers' Retirement System, \$350 million has been committed to expanding businesses in California's underserved urban and rural markets.

During the last four years at CalPERS and CalSTRS, we have committed over \$2 billion in additional capital to urban infill real estate ventures, recognizing the great opportunities that exist for housing and retail in our inner-city markets.

Our longest-lasting partnership, the California Urban Investment Partnership, to which CalPERS has committed \$290 million, has yielded an 11.1 percent annualized return since its launching in the 1990s.

Through the State Treasurer's Office, we have invested more than \$1.7 billion in Community Reinvestment Act mortgages to increase homeownership in inner-city communities. And last year, as the S&P Index dropped 22 percent, we received a yield of 6.4 percent on those mortgages.

We have increased our deposits in community banks, thrifts and credit unions – many of which are in inner city or underserved rural areas – by \$3.7 billion. We have placed funds in Chinese-American, Korean-American, and African-American banks that previously never had a dime of State money. These deposits allow these institutions to make more home mortgage and small business loans in the communities they serve.

The second pillar of our policy is based on increased diversity. At the public employees' and teachers' retirement funds, and the State Treasurer's Office, we have been working hard to diversify our investment and public finance managers to better reach out to, and succeed in, historically overlooked markets.

Michael Porter of the Initiative for a Competitive Inner City reported in an article he wrote for the Harvard Business Review that in 1977, there were about 3,000 African-Americans, Native Americans, Hispanics, and Asian-Pacific Islanders coming out of America's business schools. By the late 1990s, that number had increased to more than 15,000 a year.

There is an entire generation of immensely talented minority men and women – people seasoned in the financial world with all the skills and bona fides of the old financial order – who can be our partners and who have a unique understanding of America's growing markets. We need to make a much stronger effort to change the face of investment leadership in America for our benefit and the benefit of the larger economy.

The third pillar of this new investment dynamic is a vigorous effort by the Treasurer's Office to use limited public resources to leverage private investment. When I became Treasurer, I was stunned that billions of dollars in public funds were invested with little thought as to how we marry those resources to the engine of our vibrant private sector economy. So we are thinking differently now.

In the health field, for example, we have entered into a partnership with the National Cooperative Bank and Metropolitan Life to provide capital for community health clinics. Under our HealthCAP program, we put up \$1 of State funds as a loan loss reserve to leverage \$10 of private sector lending to build and expand clinics. Under this program, when the bank makes loans, Metropolitan Life purchases those loans, giving the bank continuing liquidity so they can make even more loans. So far, we have committed

over \$13 million to clinics which otherwise would not have had access to capital. HealthCAP is a smarter way to use public funds to strengthen underserved communities.

Let me give you another example.

To assist small businesses that have difficulty in obtaining financing, we have created a partnership with 24 lenders in our State to expand small business lending. Last year, this partnership, which we call the California Capital Access Program – CalCAP – made more than 540 loans with a focus on minority, women-owned, and inner-city businesses. Since 1999, more than \$215 million in CalCAP loans have been made to small businesses throughout California. It is a great program from our perspective because every dollar of State money results in \$23 of small business lending.

In the last year, through our three community development financial institution partners, we have begun to make what we call micro loans that help people build their own enterprises and their own future. In Los Angeles, for example, the Community Financial Resource Center lent \$500 to a person starting a graphic design service so he could buy a computer. Another \$500 went to a custom tailoring shop to purchase needed supplies. And we want to make even more micro loans because we know that participation and ownership in our free enterprise system are the best investments we can make in our future.

The fourth pillar and final pillar of our new investment dynamic is the need for all of us – local and State officials, entrepreneurs, heads of foundations, pension fund managers – to support organizations and efforts which produce the research that provides capital investors with the information they need to commit resources to inner-city ventures. The more we can spread the truth about what is really happening – the success stories of our own emerging markets – the further this dynamic can travel.

This is a critical moment for California. It is very clear to me that we have the capacity and the wealth to build a strong economy of broad prosperity where everyone has a chance to participate. The question before us is whether we have the will, and whether we are willing to make the right choices. And I believe our choices must be to educate our children, to invest in our communities, and to create a business environment that allows entrepreneurs across the class, race and economic spectrum to grow our economy, create jobs, and create wealth.

If we make these choices, we can realize the California Dream of boundless opportunity and hope.

Thank you for allowing me to speak to you today.